

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.**

In the Matter of)	
)	
Access Charge Reform)	CC Docket No. 96-262
)	
Price Cap Performance Review for Local)	CC Docket No. 94-1
Exchange Carriers)	
)	
Low Volume Long Distance Users)	CC Docket No. 99-249
)	
Federal-State Joint Board on Universal Service)	CC Docket No. 96-45

**Notice of Proposed Rulemaking
On the CALLS Petition**

REPLY COMMENTS OF THE COMPETITION POLICY INSTITUTE

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REPLY COMMENTS OF THE COMPETITION POLICY INSTITUTE

I. INTRODUCTION AND SUMMARY

Since the Commission began the process of reforming the system of access charges more than three years ago, CPI has called upon the Commission to lower the revenues that local exchange carriers (LECs) are allowed to collect for access services. From the beginning, we supported the Commission's preference for a market-based approach to reforming access charges as long as this approach employed an initial reduction in access charges and a commitment to intervene as necessary to make additional reductions if the marketplace did not do so. In our comments prior to the Commission's May 1997 *Access Reform Order*, we termed this initial reduction a "down payment" on access charge reform.¹

Following the Commission's *Access Reform Order*, the market for exchange access services has not witnessed the growth of competition sufficient to move access charges toward market levels to any substantial degree. In subsequent filings in this matter, CPI joined other consumer interests in urging the Commission to make further prescriptive reductions in the LECs' access prices.² *Especially in light of the RBOCs' imminent entry into the interLATA markets*, it is important that the Commission intervene again.

In this proceeding the Commission is presented with another opportunity to assess whether its market-based approach is working as anticipated in the *Access Reform Order*.

¹ See CPI Comments *In the Matter of Access Charge Reform*, CC Dkt. 96-262, filed January 29, 1997.

² See CPI Comments in Support of the Petition for Rulemaking of the Consumer Federation of America, International Communications Association and National Retail Federation, RM-9210 (Dec.9, 1997) (*CFA/ICA Petition*), CC Dkt. 96-262, filed January 1998.

Although the CALLS petitioners did not raise the issue of total access revenues directly, it is clear that some large IXCs do not believe the current regime is working, leading them to throw in the towel on true access reform and merely shift access revenues from carriers onto end users. But their solution spends other people's money and does not serve the interests of those most affected by the outcome — consumers. We agree with NASUCA that, as the Commission reviews the CALLS proposal, the “impact on consumers is the paramount issue in determining its merit.”³

The elements of the CALLS proposal that are most objectionable to consumers arise precisely because the proposal attempts to maintain LEC access revenue levels (or even increase them compared to what they would be otherwise). In our initial comments and again in these reply comments, CPI urges the Commission to relieve the pressures created by the CALLS proposal by ordering further reductions in access charges. In 1997 we called upon the Commission to collect a “down payment” on access charge reform. Two and one half years later it is time for the Commission to collect the next installment — a payment that is, in fact, overdue.

CPI recommends that the Commission reject the CALLS proposal because its costs to consumers outweigh its benefits. Each of the four reasons we offered in our initial comments were supported by other commenters. First, we argued that the CALLS proposal is, at best, revenue-neutral with respect to the aggregate amount of access revenues of local exchange carriers will collect. In fact, total access revenues are likely to increase over time beyond what they would have otherwise been. Second, we noted that the proposal is inconsistent with the Commission's existing policy of reducing carrier access charges by employing a market-based approach. We think it is too early to abandon that approach. Third, we argued that the plan

³ National Association of State Utility Consumer Advocates (NASUCA) comments, p. 7.

inappropriately eliminates the “X-factor” from the Commission’s price cap formula, eviscerating the theory and practice of price cap regulation. We find no justification to insulate the LECs’ access revenues from justifiable downward pressure over time. Finally, the CALLS proponents would have their solution be the final word on carrier access charges, reducing the chance that total access revenues (carrier plus end-user) will ever be reduced by future regulatory action. While this may serve the LECs’ interests, and while the IXCs may be indifferent since consumers will be paying the access bill, there is absolutely no reason for consumers to agree that the Commission put access revenues on autopilot for the duration.

Among the comments filed in response to the CALLS petition, we found ample support for our analysis that the CALLS proposal will hurt consumers.⁴ Several parties urged the Commission to reject the invitation to adopt the CALLS proposal as an “all or nothing” package.⁵ We agree and support those parties that advocate that the Commission should “cull from the CALLS proposal those elements which further its universal service and access reform objectives.”⁶ But we repeat: a revised CALLS plan is not likely to benefit consumers unless the Commission also acts to reduce the overall level of access charges.

In these reply comments we suggest a set of options the Commission can use to achieve the fundamental requirement of access charge reform, moving access charges toward competitive

⁴ See comments of the Texas Office of Public Utility Counsel (TOPUC), NASUCA, Washington Utility and Transportation Commission (WUTC), Ohio Public Utility Commission (OPUC), New Jersey Ratepayer Advocate, International Communications Association (ICA).

⁵ See Competitive Telecommunications Association (CompTel) comments, p. 7; TOPUC comments, p. 7; Telecommunications Resellers Association (TRA) comments, p. 2.

⁶ TRA comments, p. 2.

levels now. Of course, we are not offering the Commission anything brand new: all these options are laid out on the record in this proceeding. This means the Commission has a sufficient record to act on this matter now as it grapples with the CALLS proposal.

Lastly, we agree with commenters who argue that the Commission must not accept the CALLS position as a private settlement applicable only to those parties that wish to take part. If the CALLS plan or some of its elements are in the public interest, the Commission must apply those policies to all price cap LECs; any public interest benefits should flow to all consumers, not just those served by companies that agree to accept changes in the access charge regime.

II. THE COMMISSION MUST USE THIS OPPORTUNITY TO MOVE ACCESS CHARGES TOWARD COMPETITIVE LEVELS.

The most glaring defect in the CALLS plan is that it attempts to maintain the overall amount of money consumers ultimately pay in access charges. In our view, this feature of the proposal forces other effects (e.g. increased end user charges) that swamp the plan's benefits to consumers.

Many commenters agree that the CALLS plan is, at best, revenue neutral with respect to the LEC's access revenues.⁷ As TRA recognizes, "under the CALLS proposal, price cap LECs would continue to generate the same level of access revenues even as [carrier] access charges decline."⁸ Several commenters also link the maintained level of access revenue to the harm to

⁷ See ICA comments, p. 2; CompTel comments p. 13-14; MCI Worldcom comments, p. 8-9.

⁸ TRA comments, p. 6.

consumers.⁹

We are not swayed by comments that dispute the effect the CALLS plan has on net access revenue.¹⁰ Under the current access regime, access revenues are collected in the flat rated SLC, the PICC and per-minute access charges IXC's pay to LECs. In the CALLS proposal, LECs will collect an increased SLC, a flat-rated PICC (from end users instead of IXC's) and will collect lower per-minute access charges from IXC's. Further, the LECs will not face lower revenues since total revenues are buffered by a \$650 million universal service fund. Finally, the eventual elimination of the productivity X-factor means that access revenue levels, (by that point collected mainly from end users) will increase at the rate of inflation, unhampered by the fact that LECs will continue to experience large productivity gains.

All these considerations point to one conclusion: fairness to consumers demands that, whatever elements of the CALLS proposal are retained, the Commission must modify the proposal and move access rates toward competitive levels by prescriptive reductions.

A. The Commission Has Ample Evidence That Rates Are Excessive.

The CALLS plan incorrectly assumes that the existing level of access revenues are based on *bona fide* costs necessary to support the LECs universal service obligations.¹¹ While this argument might have had more claim to truth in a regulated monopoly world where regulators examined only reported accounting costs and did not even consider economic costs, it is

⁹See MCI Worldcom comments pp. 8, 14-15; CompTel comments p. 14, Time Warner Telecommunications (Time Warner) comments, p. 7.

¹⁰ See CALLS comments, p. 18.

¹¹ See CompTel comments, p. 15; MCI Worldcom comments, p. 8-9.

unsustainable now. Despite the claims of incumbents about their right to collect these historic costs, the gap between legacy costs and forward-looking economic costs is real and represents the “overhang” garnered by an industry not subject to competitive pressures. The world has changed.

Parties to this proceeding offer numerous reasons why existing access revenues are inflated.¹² First, there are historic costs embedded in access charges,¹³ there are costs embedded in the price cap index and access charge rates that reflect nonexistent or overbuilt infrastructure,¹⁴ and the price cap productivity factor is understated.¹⁵ We agree with these analyses and also note that the rate of return on equity incorporated in the original price cap plan assumptions is far in excess of today’s market returns.

B. Reducing Access Revenues at this Time is Consistent with *Access Reform Order*

In its *Access Reform Order*, the Commission determined to employ a combination of market forces and prescriptive measures to move access charges to competitive levels. The central effect of the CALLS proposal is to surrender in that effort and merely shift access revenues from carriers to end users. It is easy to see the appeal of this approach to the CALLS participants: the LECs dispose of the threat that either the market or the Commission will force reductions in access revenues; the IXC’s shift the problem off their plate and onto their customers.

¹² See TRA comments, p. 7.

¹³ See *Access Charge Reform Order* par 258-284.

¹⁴ See CPR Audits for Ameritech, Bell Atlantic North (NYNEX), Bell Atlantic South, Pacific and Nevada Bell, Southwestern Bell, BellSouth and US WEST. 14 FCC Rcd 7019.

¹⁵ See MCI Worldcom comments, p. 16. See also the record evidence in CC Docket Nos. 94-1 and 96-262.

We do not think the Commission should follow the CALLS signatories and abandon the course it set upon in its *Access Reform Order*. As long as the Commission retains its resolve to make prescriptive reductions if needed, we think the Commission was right to conclude that market forces will eventually produce access charges at competitive levels. The CALLS proposal comes along at a time when the Commission must contemplate doing what it said it would do: by reducing access charges further now, the Commission can move the reform process back on the track laid out in the *Access Reform Order* and, in the process, consider some of the reforms embodied in the CALLS proposal.

The Commission has ample evidence that market forces have not yet had an impact on access charges.¹⁶ As if to bolster that conclusion, the fact that some large IXC and large ILECs can agree on the CALLS proposal means that these IXCs do not believe market forces alone will bring access charges close to economic costs in the next five years. These events recommend an obvious course for the Commission: it should restore faith in its preferred approach by following through on its promise.

C. The Commission Has a Range of Options to Prescriptively Reduce Level of Access Charge Revenues.

In several proceedings, all captioned in this docket, CPI and other parties have offered suggestions on ways to justify significant reductions to the existing level of access revenue.¹⁷ These include increasing the X-factor to reflect higher interstate productivity levels, applying the corrected X-factor to the entire period of time in which this round of price caps regulations have

¹⁶See ICA comments, p. 4; *See e.g., CFA/ICA Petition*.

¹⁷ *See generally* CPI comments in *CFA/ICA Petition*; *See also CFA/ICA Petition*.

applied, reinitializing the price cap index and incorporating a true market-level rate of return in the underlying price cap levels. We do not need to reiterate the technical arguments here, some of which were reprised in comments filed in this docket. For example, MCI Worldcom suggests reinitializing the price cap index based on the results of the CPR audits,¹⁸ and recalculating a higher X-factor on a retroactive and forward basis.¹⁹ We also note that the ever-increasing return on investment reported by the price cap LECs demonstrates the reasonableness of revising the price cap regime. After all, price caps are supposed to produce outcomes that mimic the outcomes of competitive markets in which only market-level returns on capital are achieved in the long run.

CPI agrees with CompTel's suggestion that the Commission immediately revise access rates rather than wait for the schedule set forth in the CALLS plan.²⁰ Indeed, if the Commission uses this opportunity to reduce overall access charge levels, it can immediately deliver the purported benefits of the CALLS plan without increasing end user charges.

CompTel makes two other points we wish to highlight. First, we agree that, contrary to the CALLS plan, the target levels for switched access rates "cannot be allowed to function as a floor on access charge reductions."²¹ The proposal to use those targets as a floor contradicts the Commission's stated policy of bringing access charges to forward-looking costs. Second, CPI agrees with CompTel that there is no sound rationale for giving price cap LECs more time to

¹⁸ See MCI Worldcom comments, p. 15.

¹⁹ See *Id.*, p. 16.

²⁰ See CompTel comments, p.13-14.

²¹*Id.*, p. 13.

reduce their rates to cost.²² CompTel is correct that these carriers “have been on notice for many years that current access charge levels are unsustainable” and that the Commission’s goal is bringing those charges to “levels that reflect underlying economic costs”²³

III. ANY MODIFIED CALLS PLAN MUST APPLY TO ALL PRICE CAP LECs

In its petition, CALLS suggests that the Commission could implement the CALLS plan for signatories while maintaining the current access charge and universal service regime for those price cap LECs and IXC that choose not to accept the CALLS proposal. We think this would be a serious policy error for the Commission to make. CPI agrees that it would be improper to adopt the CALLS plan under that “opt-in” framework.²⁴ The Commission should not adopt a plan that creates a bifurcated price cap regulation plan and a bifurcated (actually *trifurcated*) universal service plan, one for CALLS LECs, one for non-CALLS LECs and a third one for rural LECs.

If the Commission determines that the CALLS plan serves consumers, it has the obligation to see that all consumers have the opportunity to benefit. As matter of national policy, the Commission should not offer two separate sets of rules for similarly situated carriers simply because one carrier likes the rules or the rulemaking process and the other one doesn’t.

Furthermore, such a split regime would make it difficult for IXCs (especially those who were not signatories to the plan) to develop national, regional, or even statewide strategies for

²² *See Id.*

²³ *Id.*, p.13-14.

²⁴ *See Id.*, p. 7.

marketing services. In some states, for example, consumers would be served by a CALLS LEC (say, GTE) while others might be served by a non-calls LEC (perhaps US WEST). In such an example, an IXC would operate under two quite different access systems. Consumers of the two LECs would pay the same IXCs different flat PICC charges and different per-minute rates. IXCs would presumably need separate billing systems for its customers in those LECS areas. In the CALLS LEC area, for instance, the IXC would not bill the consumer a PICC (either through a separate charge or incorporated into its per-minute rate) while in the non-CALLS LEC area it would need somehow to factor the flat rated cost of access into its rate or into a separate line item billed to the end user. Clearly a dual system of price cap regulation could confuse consumers and present additional costs to the carriers.

We are likewise concerned that a dual price cap regime might force IXCs to offer average prices nationwide in such a way that some consumers would subsidize others. As CompTel suggests, IXCs might have to offer a nationwide price that includes their cost of access in states where they obtain access from non-CALLS LECs.²⁵ In other words, some consumers might never see the lower rates the CALLS signatories promise even if their LEC was a party to CALLS.²⁶ The best way out of these difficulties is to apply any revised access charge regime to all price cap LECs uniformly.

²⁵ *See Id.*, p. 9.

²⁶ *See CALLS comments*, p. 4.

IV. Conclusion

After reviewing the comments of other parties in this matter, we remain convinced that the shortcomings of the CALLS proposal outweigh its merits. We reiterate our position that the Commission should deny the CALLS petition unless substantial changes are made. Chief among these necessary changes is the need for the Commission to make another prescriptive reduction in total access revenue levels. To the extent it does so, many of the consumer objections to the CALLS proposal diminish.

Respectfully submitted,

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Certificate of Service

I, Joshua M. Bobeck, hereby certify that on this third day of December, 1999, copies of the foregoing Reply Comments of the Competition Policy Institute were served by electronic filing or by first-class, United States mail, postage prepaid, upon each of the parties listed below.

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